

## ANALYSIS OF ORIGINAL BILL

Author: Alquist Analyst: Gloria McConnell Bill Number: AB 1662

Related Bills: See Legislative History Telephone: 845-4336 Introduced Date: 01/12/98

Attorney: Doug Bramhall Sponsor:

SUBJECT: Unpaid Child Support Credit/Single Parent Protection Act of 1998

### SUMMARY

Under this bill, taxpayers entitled to receive child support payments would be allowed a tax credit equal to the amount of unpaid child support. The credit would be allowed only if the taxpayer includes the name and taxpayer identification number of the person required to make the child support payments. When a credit for unpaid support is allowed, the tax of the person required to make the payment would be increased by the amount of the credit.

### EFFECTIVE DATE

For taxable years beginning on or after January 1, 1999, and before January 1, 2004.

### LEGISLATIVE HISTORY

AB 1395 (Stats. 97, Ch. 614).

### PROGRAM HISTORY/BACKGROUND

Federal law requires each state to have a single agency responsible for enforcing child support, but permits delegation of specific tasks to local levels. The Department of Social Services (DSS) is designated as the California state agency. By state law, the county district attorneys (DAs) are delegated responsibility for enforcing child support, which includes collecting current payments and delinquencies. Typically the custodial parent is entitled to receive the support payments on behalf of the child. Prior to commencing the child support enforcement process, judicial action is required. Once an ordered amount becomes delinquent, DAs are required to search for assets of the obligor and take collection actions as necessary to collect the delinquent account.

In 1993 (Speier, AB 3589; Stats. 92, Ch. 1223), Franchise Tax Board (FTB) began collecting delinquent child support through a pilot project in which DAs in six counties could voluntarily refer their delinquent child support accounts to FTB

### DEPARTMENTS THAT MAY BE AFFECTED:

\_\_\_ STATE MANDATE

\_\_\_ GOVERNOR'S APPOINTMENT

Department Director Position:

\_\_\_ S \_\_\_ O  
\_\_\_ SA \_\_\_ OUA  
\_\_\_ N \_\_\_ NP  
\_\_\_ NA \_\_\_ NAR  
\_\_\_ X \_\_\_ PENDING

Agency Secretary Position:

\_\_\_ S \_\_\_ O  
\_\_\_ SA \_\_\_ OUA  
\_\_\_ N \_\_\_ NP  
\_\_\_ NA \_\_\_ NAR  
DEFER TO \_\_\_

### GOVERNOR'S OFFICE USE

Position Approved \_\_\_  
Position Disapproved \_\_\_  
Position Noted \_\_\_

Department Director

Gerald H. Goldberg

2/23/98

Agency Secretary

Date

By:

Date:

for collection as though they were delinquent personal income taxes. In 1995, the program was expanded to include voluntary referral from all counties (Speier, AB 923; Stats. 94, Ch. 906). This year, effective on January 1, 1998, DAs are required to refer all child support obligations that they are responsible for enforcing that are 91 days or more delinquent to FTB for collection as though they are delinquent personal income taxes (AB 1395, Escutia; Stats. 97, Ch. 614). Additionally, DAs can voluntarily refer those child support delinquencies that are less than 91 days delinquent to FTB for collection as though they are delinquent personal income taxes. In the event an individual owes both delinquent tax collection and child support referred to FTB for collection, tax collection activities generally take priority over those for child support collection.

FTB uses all the collection remedies and information sources to collect delinquent child support that it uses to collect tax debts. FTB collections are transferred within several days to the DAs, who forward the amounts to the families or the state, as appropriate. Each month the DAs notify the FTB of the amount of the child support delinquency subject to collection.

For the period July 1, 1997, through December 31, 1997, FTB collected approximately \$12 million in delinquent child support for non-welfare cases and \$17 million in delinquent child support for welfare cases.

California is required under federal mandate to have a statewide child support enforcement system and centralized payment and disbursement unit, which are the responsibility of DSS. Implementation is currently under consideration.

#### SPECIFIC FINDINGS

**Under current law**, child support payments are not a taxable event. Payments are not treated as income to the custodial parent or deductible from the obligor's adjusted gross income.

**Under this bill**, the eligible individual (custodial parent) would be allowed a credit against tax for an amount equal to the unpaid child support, as defined, for the taxable year, and the tax of the person required to make the payment (obligor) would be increased by the amount of the credit. To be allowed the credit, custodial parents must include on their tax return the name and taxpayer identification number of the individual required to make the payments. The unpaid child support would not apply to support that has been assigned to the state as a condition for receiving aid for needy families.

The increased tax cannot be treated as tax for purposes of determining the amount of any other credit or the alternative minimum tax.

#### Policy Considerations

According to discussion with the author's staff, this bill mirrors language from a proposal at the federal level, which has not begun to move through the federal legislative process. However, for the reasons provided below, the author's staff recognizes this bill as currently drafted may not achieve the author's intent of (1) providing a more immediate benefit to these custodial parents than the customary child support collection avenues and (2) create a revenue neutral impact to the General Fund:

- Those custodial parents with limited taxable income would receive little or no benefit from the tax credit. For example, a custodial parent who is entitled to unpaid support of \$1,800, files as head of household, has one dependent and claims taxable income of \$16,800, would have a net tax of only \$100. Hence, even though the unpaid support and resulting allowable credit would be \$1,800, the custodial parent would be allowed to benefit from only \$100 of the allowable credit, which is the amount equal to the net tax. In order for a head of household custodial parent with one dependent to be able to use a \$1,800 unpaid child support credit, that parent would have to have taxable income in excess of \$48,050.
- Revenue neutrality may not be achievable because some obligors may be unemployed, receiving public assistance, disabled, incarcerated or otherwise unable to pay the assessment in the near future, if ever. In the case of obligors living out-of-state, the state's ability to assess and collect this new tax may be questionable if California lacks taxing jurisdiction (nexus).

#### Implementation Considerations

The following implementation issues have been identified:

- When the name and taxpayer identification number of the obligor is provided on the custodial parent's tax return, it is unclear whether the author intends for the obligor to have protest rights before the increase in tax is final and due and payable. Without protest rights, it could be argued that due process has not been given. Through the protest process, it may be found that the credit was incorrectly claimed. In which case, it is presumed, but unclear, that the previously allowed credit should be disallowed.
- There may be occasions where the custodial parent does not know the social security number/"taxpayer identification number" or the name of the absent parent or provides incorrect information. Without correct and complete information and the ability to readily verify the correctness of the information, collection of the assessable amount would be hindered. Collections also would be hindered if FTB does not have or cannot locate an address of record for the identified obligor.
- The credit under this bill is allowed to individuals who are "entitled" to receive child support payments and have not received the payments for that year. Perhaps there are custodial parents who believe they are entitled to receive child support payments, but the belief is not sanctioned by the court or other legal documents or proceedings. The definition of "entitled" would need to be clarified.
- It is unclear how FTB would readily verify that child support is due and unpaid for a specific year. FTB does receive limited data on child support delinquencies from counties for its current child support collection program, but the data are insufficient to establish an efficient verification system for three reasons: 1) San Diego County is

exempted from FTB's program, 2) not all child support delinquencies are referred to DAs for collection, and 3) FTB does not receive the amount of the child support delinquency on a year-to-year basis. Additionally, there may be system constraints as FTB child support system is designed primarily to expedite the processing of automated collection actions (wage garnishments and bank levies).

Under federal law, California is required to establish certain centralized child support systems (Statewide Automated Child Support System [SACSS] and a centralized collection and disbursement unit). However, according to DSS the schedule and plan for implementation for these systems is still under consideration. Also, even under these systems, it is uncertain whether information would be available on a year-to-year basis or whether current law would permit the use of the information for tax enforcement purposes, which would include administration of the custodial parent's credit and offsetting tax from the obligor.

- In the event the unpaid child support is subsequently collected through the DA/FTB child support collection programs or voluntarily paid by the obligor, the custodial parent would have received both a credit for and the payment of the same previously unpaid amount. Additionally, the obligor would have two debts for the same previously unpaid child support, the child support delinquency that was collected or voluntarily paid and the tax liability that resulted from the allowed credit. The author's staff has indicated that there is no intent to provide a double benefit for the custodial parent or a double debt for the obligor.
- This bill conflicts, in part, with FTB's current child support program. FTB would be in the position of trying to collect the child support delinquency via referral from the DA, generally at the same time it also would be increasing the obligor's tax debt from the same child support delinquency. Because tax collection by FTB has priority over child support, FTB would forgo collection of the child support delinquency, which could include arrearages not covered by the credit, until the tax debt created by this bill is satisfied. Again, according to the author's staff, there was no intent to interfere with collection of the unpaid child support.
- The bill precludes the increased tax passed on to the obligor from being used to determine the amount of any other credit. However, the amount of a credit is determined by the taxpayer's particular expenditure, and the amount of the credit that can be claimed is determined by the amount of tax liability. Therefore, it is unclear whether the intent of this provision is to prohibit the reduction of this increased tax amount by the using the other credits that are available for tax purposes, e.g. personal exemption credit, adoption costs credit, or business related credits.
- Penalties are imposed, including the estimated tax penalty, when taxes are not paid by the due date for that tax, which is generally April 15<sup>th</sup> following the close of the taxable year. Interest accrues on unpaid tax from the due date. Interest on penalties accrues from the date the

penalty is assessed and due and payable. As the bill is drafted, it appears this general rule for penalties and interest on taxes would apply and they would apply as of April 15<sup>th</sup>, regardless of when the new tax is actually assessed. However, considering that the new "tax" would be assessed only after the custodial parent claims the credit, it is unclear whether the general penalties and interest provision is intended to apply.

#### Technical Considerations

The following technical considerations have been identified:

- This credit applies to any individual to whom child support payments have not been made. The individual could be presently married and filing a joint tax return. However, the name of the act (Single Parent Protection Act of 1998) implies it should be limited to only those individuals who are other than married as of the last day of the calendar year during which the amount was unpaid.
- To receive the credit under this bill, the custodial parent must provide the "taxpayer identification number." For taxpayers who are individuals, which would be the only taxpayers subject to this bill, FTB relies on the social security number for enforcement purposes. It is suggested that "social security number" replace the term "taxpayer identification number."

#### FISCAL IMPACT

##### Departmental Costs

Administrative costs cannot be determined until the implementation considerations are resolved.

##### Tax Revenue Estimate

Because of many implementation concerns, it is not possible to estimate the bill's impact. However, it is known that the average monthly child support obligation is estimated to be \$362 (approximately \$4,300 annually) for which potential credits could result. It is estimated that currently there are over one million delinquent child support cases in California. This total includes all cases with support orders including cases that have not been assigned to district attorneys for collection.

It is very likely that significant net revenue losses to the state would result due to the application of the tax credits without offsetting collectible tax assessments.

#### BOARD POSITION

Pending.